January 30, 1998

Ms. Mary Cottrell, Secretary
Department of Telecommunications and Energy
100 Cambridge St., 12th Floor
Boston, MA 02202

REFERENCE: D.P.U./D.T.E 96-100, Electric Industry Restructuring,
220 C.M.R. Section 11.06, Information Disclosure Requirements

Dear Ms. Cottrell:

On Friday, January 16, the Department of Telecommunications and Energy (DTE or Department) issued draft regulations governing the restructuring of the electric industry. Section 11.06 of the draft regulations pertains to Information Disclosure Requirements and is the focus of these comments.

We applaud the hard work that is evidenced in the DTE draft. The DTE has established the outline for a disclosure system which can, if certain important changes are made, help to usher in competition in the electricity market. Nonetheless, we feel very strongly that the State and the people of Massachusetts would be better served if the DTE would reconsider its positions on several significant issues based on the recommendations and explanations we outline below.

It is our considered opinion that, despite the Department's best intentions, the practical effect of the regulations it has drafted will be to impose inefficiencies on the market, drive up the cost of electricity, cripple the market for renewable resources, reduce potential environmental improvement in the state, and risk delays and disruption from litigation. We believe it is also fair to say that the combined effect of these drawbacks, should they not be remedied in the final regulations, would directly conflict with the purposes of the legislature expressed in the Restructuring Act.

We reiterate here the basic criteria by which we feel any disclosure system should be assessed:

(1) does the disclosure label facilitate "apples-to-apples" comparisons for consumers;
(2) does the information in the label help consumers more clearly understand the characteristics of the offer being made to them and protect them from deceptive claims;
(3) does the disclosure system "encourage innovation," "provide incentives to operate efficiently," "open markets for new and improved technologies," and "allow market forces to play the principal role in determining suppliers" as required by the Restructuring Act;
(4) does the disclosure system "enhance environmental protection goals," as required by the Restructuring Act;
(5) is the disclosure system feasible -- i.e., can the information needed for the

label be collected, calculated and delivered in the manner prescribed by the rules;

(6) are the burdens for administering and complying with the disclosure system reasonable and equitably distributed;

(7) does the disclosure system comply with the legislative intent and with other laws and legal principles; and

(8) recognizing that restructuring will reveal new lessons about competitive markets and that there will be a certain degree of upheaval in the way electricity markets work during the start-up phase, is the disclosure system simple to comply with, is it flexible enough to adapt over time, and does it avoid placing complicated and burdensome procedures on market participants and the ISO.

These criteria form the basis of our analysis and lead us to recommend the attached changes to the draft DTE regulations which we urge you to consider. We also note that the detailed draft regulations proposed by the Department of Energy Resources (DOER) and filed with the Department on January 9 present a model from which guidance and language might be drawn with regard to most of the issues discussed below. We further request that the Department initiate an emergency forum or "technical sessions" in which stakeholders can work with the Department staff to help design the necessary modifications to the DTE draft regulations. Given the magnitude of the work that remains to be done, we feel that a collaborative effort offers the best chance for devising a workable disclosure system in time for final approval and implementation in compliance with the timeline initially forecast in the Order of January 16, 1998.

The signatories to this letter thank the DTE for the opportunity to comment on these important issues.

I have been authorized to sign this document on behalf of those listed below.

Respectfully submitted,

/s
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For the Conservation Law Foundation

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Attachment

Comments on Massachusetts DTE Draft Disclosure Rules
220 C.M.R. Section 11.06

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1. Product-based disclosure -- The information contained in disclosure labels must be product-based, not company-based

We recommend changing the basis of disclosure so that what the customer sees in the label are the characteristics associated with the product being offered, not the resource portfolio of the company that is offering the product. Section 11.06(2)(d) should simply replace the term "Load-serving Entity" (LSE) with the term "price offering." Subsection (2)(d)1.(a) should further replace all references to LSEs in the first sentence with the term "price offering," as should all of subsection (2)(d)1.(b).

The reasons for making this change are clearly enumerated in the comments being submitted by the DOER and are generally endorsed by the signatories here. We take this opportunity to briefly review our position on the issue.

Our first argument in favor of product-based disclosure is that it conforms with the express objectives of the Restructuring Act. For example, Section 50 states that Section 11D of the Act should be amended to authorize and direct the commissioner "to assist consumers in understanding and evaluating their rights and choices .... (in a way that) shall provide consumers with information that provides a consistent and reliable basis for comparing products and services offered in the electricity market..." (Emphasis added).

Second, the result of company-based disclosure unreasonably impedes retail suppliers' ability to differentiate and market their products. Suppliers of electricity, who had hoped to offer customers a variety of products to choose from, will be forced under the company-based approach to attach a label that makes all of their products look identical. Suppose, for example, a supplier wishes to offer two products. The first is its "Low Price" offer in which a flat rate of 3 cents per kWh will buy electricity 100% of which is derived from a group of coal plants. The second offer is for a product that costs more, but is derived 80% from renewable energy resources and 20% from natural gas, and therefore has very low emissions associated with it. Under the company based approach, and assuming each product comprised half of the supplier's total load, the characteristics of these two products would be averaged together. The label for the renewable product would show that it contains 50% coal and has significant emissions, while the label accompanying the coal product would indicate it is half renewables and natural gas, and has far lower emissions than are in fact associated with the product's generation.

This is a concern for all market participants and for Massachusetts customers seeking the best products and the lowest prices. The legislature made clear its preference for using market forces to achieve competition when it declared that: "competitive markets

in generation should (i) provide electricity suppliers with the incentive to operate efficiently, (ii) open markets for new and improved technologies, [and] (iii) provide electricity buyers with appropriate price signals..."; and that "market forces [should] play the principal role in determining the suppliers of generation for all customers." Restructuring Act, Section 1(g) and (k).

While detrimental to market participants and consumers generally, the DTE approach is devastating for suppliers of environmentally preferable products in particular. Here again the DTE approach seems to employ an outdated view of how markets will operate[1] and to contravene the goals of the legislature. For example, the Restructuring Act establishes a fund to support renewable energy markets and, in Section 68 proposes adding Section 4E(c)(i) such that:

> Public interests to be advanced ... shall include, but not be limited to, the following: (i) the development and increased use and affordability of renewable energy resources in the commonwealth and the New England region; (ii) the protection of the environment and the health of the citizens of the commonwealth through the prevention, mitigation, and alleviation of the adverse pollution effects associated with certain electricity generation facilities; (iii) the delivery to all consumers of the commonwealth of as many benefits as possible created as a result of increased fuel and supply diversity; (iv) the creation of additional employment opportunities in the commonwealth through the development of renewable technologies; (v) the stimulation of increased public and private sector investment in, and competitive advantage for, renewable energy and related enterprises, institutions, and projects in the commonwealth and the New England region; and (vi) the stimulation of entrepreneurial activities in these and related enterprises, institutions, and projects. (Emphasis added).

[1] As drafted, the Resource Portfolio section appears to contemplate a universe in which all suppliers are either NEPOOL participants or buy system power from NEPOOL participants. In the new competitive markets, suppliers may choose to contract with NEPOOL participants for specific, traceable resources. We urge the DTE to clarify the Resource Portfolio provisions so that suppliers having such contracts are able to distinguish their resource mix from that of the pro rata share of the participant with which they contracted.

In effect, the DTE approach defeats the hopes many held that restructuring would lead to environmental benefits. In the illustration used above, it is likely that some customers will think the two products are identical except for the price. In this case, they will certainly choose the cheaper of the two, which means that more existing coal power will run in Massachusetts at the expense of new renewables or other cleaner resources. Obviously, this result will be particularly detrimental to would be marketers of environmentally preferable products. It will frustrate the legislature's hope that restructuring would "enhance[] environmental goals" over time by creating a market shift to renewable products that would displace older, dirtier generation and would dramatically improve the air quality in Massachusetts and New England. By limiting the ability of these products to be developed and marketed, the DTE's approach will reduce the likelihood that we will see environmental benefits associated with restructuring.

From a consumer protection standpoint, it is also clear the company-based approach is not desirable. The illustration above shows how difficult it will be for customers to make "apples-to-apples" comparisons, a stated goal of regulators, consumer protection advocates and market participants since discussions on disclosure first started. This view is supported by Section 193 of the statute, which provides that Section 1F(6) be amended so that "The department shall require that such an electricity information label provide prospective and existing customers with adequate information by which to readily evaluate power supply options available in the market."

Several critics of the company-based approach have suggested that suppliers will try to evade the drawbacks of the approach by forming subsidiaries or individual, product-based settlement accounts. While this might solve some of the problems noted above, it will certainly dilute efforts of suppliers to "brand" their products in the marketplace and will add unnecessary costs to doing business which will be passed on to consumers. The proliferation of small companies that may result would also add a significant burden to the market settlement systems of the Independent System Operator (ISO), an outcome that cannot be desirable particularly when the ISO is so busy during the first stages of restructuring. Moreover, we feel the DTE should be concerned that such a proliferation will unnecessarily burden the DTE with added licensing duties.

Finally, from a legal perspective the DTE approach also poses significant problems. Because the information on the label will likely conflict with information contained in adjacent marketing materials, the labels may inadvertently mislead customers. In so doing, the labels will almost certainly run afoul of federal and state deceptive advertising laws. A disclosure scheme that forces businesses to make statements that are false or misleading faces a very serious risk of being invalidated on the grounds that it violates the First Amendment doctrine on commercial free speech.

We strongly feel that the product-based alternative will cure the problems we have noted above and will not add any unreasonable burdens or risks.

2. "Auditable Contract Path" -- The definition of "Known Sources" should be expanded so as to enable suppliers to include in their label any characteristics they purchased by way of an "auditable contract path."

We strongly urge the DTE to revise Section 11.06(2)(d)1.(c) to clarify that Known Resources will include resources associated with generation in which the supplier holds "evidence sufficient to establish an auditable contract path." We further suggest that Section 11.06(2)(d)1.(b) replace the words "generating unit ownership and contracts" with the word "resources."

It appears from DTE's definition of "Known Resources" that no marketer who uses any power derived from system power contracts that draw power from a defined group of units identifiable by auditable contract path in order to reduce financial risk and overall costs) may register the characteristics of this power in their labels. If read this way, the DTE's rules will further inhibit a marketer's ability to offer an accurate, meaningful characterization of its products, and will significantly add to the cost of participating in the market, especially for suppliers of renewable energy resources.

We think it highly desirable for any disclosure system in New England that suppliers, and those offering environmentally oriented products in particular, have access to the efficiencies of purchasing energy from unit-contingent or tailored system power contracts. They should not be prevented from claiming in their ads or their labels certain attributes of that power so long as it can be proved that the attributes were in fact generated, in an amount certain, that it was allocated to the LSE, and that this amount was not allocated to anyone else (i.e., it was not double sold). The DOER draft definition of Specified Resources would satisfy our concern. There, a Specified Resource (or "Known Source") is defined as "the fuel type or other energy input used by a generating facility that provides all or part of the generation for a [price] offering pursuant to a unit contract, a unit-contingency contract, a unit entitlement, unit ownership, <u>or a system power contract under which the generation facility (or facilities) are identifiable by an auditable contract path</u>." (Emphasis added). Such an approach would dramatically reduce costs for providers of renewable energy and would reduce financial risks. This in turn would make renewable energy more competitive and, presumably, would enhance the level of environmental benefit resulting from the restructuring process.

A standard very similar to the one we propose here has been adopted as part of the disclosure regulations in California and was also recommended in the RAP report on the New England Disclosure Project as well as in the DOER draft regulations. These other forums found solutions to tracing generation sources in a way that could keep costs to a minimum and reassure consumers that power characteristics (e.g., labor practices or environmental benefits) are not being exaggerated or double counted. By contrast, DTE's approach appears to force anyone wishing to claim a high level of labor or environmentally preferable characteristics to meet the claim with the blunt instrument of certain unit contracts. The same claims could reasonably be met with greater flexibility and cost savings by way of system contracts where the sources of generation are traceable through a carefully defined "auditable contract path."

Finally, many renewable resources (hydro, wind, solar, landfill gas), historically treated as "loads carried," are either too small (less than 1 MW) or are located on customer premises, such that their generation may not appear directly on ISO settlement records. Nonetheless, we feel that if these resources have an auditable contract path it is appropriate to include them in the label.

3. Settlement Period -- The settlement period for calculating the attributes of a price offering's resource portfolio should be extended to a reasonable period of time (e.g., quarterly, semi-annually, annually), not hourly.

We recommend that the method for determining the resource portfolio and known resources be clarified to allow settlement of energy characteristics over a reasonable, extended period of time. To accomplish this change, subsections 11.06(2)(d)1(a) and (c) should be revised such that the resource portfolio does not rely exclusively on hourly settlement data from the ISO. The draft DOER regulations that were filed with DTE on January 9 may offer some guidance on how best this can be achieved. In short, the DOER draft suggests allowing marketers to add up the sum of its entitlement to generation characteristics traceable through "Known Resources" (variously referred to as "Specific Sources" or "Specific Purchases") at the end of the closing period and then allocating the characteristics as needed to meet its claims.

The DTE approach to tracing the characteristics associated with a product unnecessarily and unreasonably restricts the ability of suppliers to develop products and significantly increases the expense of bringing products, especially environmentally preferable products, to market. Such added expense may make renewable resources too expensive to compete in the market.

The problem with relying exclusively on hourly settlements is that certain desirable energy characteristics, including the use of "intermittent" renewable resources such as run-of-river hydro, wind, and solar power, cannot efficiently be controlled as to when they run. Thus, if a river happens to be full after a period of heavy rain and generates electricity in

excess of the supplier's load, the surplus will be sold into the power pool. Under the DTE's use of hourly settlements, the ISO would show that the generator only provided as much hydro as was needed to meet its load. The surplus hydro characteristics would be assigned the characteristics of the residual pool and would thus be wasted. The supplier entitled to the hydropower would not be able to "bank" or "save" the surplus hydro for use during periods when river flows are down, which means it would have a more difficult and costly job of purchasing enough of the characteristics it needs to meet its product offerings. Concerns may be even greater for resources like wind. In short, the practical effect of this approach rejects the legislative goals to "encourage innovation," "open markets for new and improved technologies" and "enhanc[e] environmental protection goals." Restructuring Act, Section 1, (f), (g) and (l).

Finally, we have serious concerns that the DTE reliance on hourly settlements may overburden the efforts of the market participants and the ISO with regard to capturing, calculating and transmitting all the data needed to complete the labels. We feel that the DTE has an obligation to publicly confirm that the ISO has the necessary authorization, funding and technical capacity to implement DTE's proposed rules and procedures without delaying or seriously complicating the opening of markets by the scheduled date of March 1.

4. Advertising -- (a) Disclosure labels should be required on specifically defined written marketing materials, not "all written marketing materials," and (b) suppliers should be allowed to advertise to the full extent of their rights within the parameters of the Federal Trade Commission Act and Ch. 93A of the Massachusetts General Laws on deceptive advertising.

We recommend first that Section 11.06(6)(b) be modified so that marketers are not required to place disclosure labels in "all written marketing materials." Quite simply, this may have the unintended consequences of chilling free speech. To illustrate the point, suppose that a marketer wishes to purchase a small ad in the Sunday edition of the Boston Globe to proclaim that it is an environmentally sensitive company, that it offers a variety of products in the new market, and that more information can be obtained at a toll free number. The cost of buying enough space to provide the disclosure information required by the DTE regulations will be prohibitive, and will adversely impact all but the largest and best financed suppliers. Judicial opinions from the Supreme Court and the Second Circuit on precisely this point suggest that overbroad disclosure requirements will be susceptible to First Amendment challenge. In lieu of the provision drafted by DTE, we urge consideration of the criteria for label placement contained in the DOER draft regulations. These criteria ask whether an advertisement (a) includes a claim with respect to any of the types of information that appear on the label and (b) incorporates a means for customer application for a particular generation offering."[2]

[2] We interpret this to mean that a newspaper ad containing a coupon that can be clipped and sent to the supplier as a means of signing up would require a label.

Second, we recommend clarifying Section 11.06(6)(d). As currently written, this provision might be read to suggest that no claims may be made about a company's or product's environmental characteristics unless it surpasses the RPS and GPS standards. As a preliminary matter, we seek clarification and assurance that environmental claims may be made before the year 2003 when these standards first take effect.

5. Contingency System -- If necessary to avoid delays or other complications in the implementation of disclosure, the DTE could rule that LSEs must disclose information about fuel source, emissions and labor characteristics of Known Resources only to the extent that a claim about the characteristic is made. Where no claim is made, default values would be acceptable.

The Restructuring Act and the DTE regulations foresee that information must be disclosed for each price offering. We recognize, however, that it may be desirable to adopt a simplifying convention in order to provide fuel mix, emissions and labor information in the event that capturing these components of the disclosure regulations meets with unexpected implementation complications. Under such a convention, the label, when it appears, would continue to present the price and contract information as currently envisioned. During the contingency phase, however, suppliers would be required to disclose the characteristics of Known Resources only to the extent they make a claim about the fuel mix, emissions or labor practices. To the extent no such claim is made, the label would ascribe the default characteristics of the residual system mix as described in 11.06(2)(d)1(d).

The main benefit of employing such a contingency system is that it would significantly alleviate the burdens, costs and confusion associated with tracking settlements and calculating the associated characteristics. This would free up the ISO to focus all its energy on the job of overseeing the myriad new procedures and duties of the new competitive market. As for suppliers, those who wish to differentiate their products by highlighting environmental or labor characteristics could do so and would be on notice that collection and calculation of data was necessary in order to substantiate their claims.[3] Those who do not make a claim about the environmental or labor attributes of their product would not be forced to do so. The DTE has suggested that administrative simplicity and reduced costs are arguments in favor of company-based disclosure system, and we feel those goals could be much better achieved, with no perceivable drawbacks, by easing the criteria for which all Known Resources would be tracked and reported during the first months of competition.

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[3] We further request the DTE to offer additional guidance on how market participants are supposed to collect and calculate labor characteristics and who will calculate the residual mix. We are concerned that it may be difficult under the current draft provisions, especially for traders and for environmentally oriented marketers (who will be making purchases strictly based on environmental characteristics known to them) to determine "whether a majority of employees operating at plants are employed under collective bargaining agreements," and "whether any replacement workers were hired" in the past year.

The policy risks of such a contingency system are negligible. Environmental protection goals will be adequately met. The difference between a product derived from high-emissions Known Resources and the default residual mix will be little or nonexistent. Indeed, we expect that most consumers who opt not to select a product that affirmatively claims to have environmental benefits will be looking merely at price to make their decision. In this case, the fact that the other characteristics indicate the residual mix instead of actual mix will be irrelevant to their purchasing decision.

Similarly, consumer protection goals are satisfied under the contingency approach. The main information on price and contract terms will always be present. And a required minimum of information about the characteristics of New England's fuel mix, emissions and labor practices will also be presented, which will raise the general level of awareness and sophistication among Massachusetts consumers and will help them make more informed decisions when better information becomes available.

Finally, regulators, market participants and Massachusetts consumers should all take considerable comfort in the fact that all claims made about the characteristics of an electricity offering will be subject to Massachusetts deceptive advertising laws and regulations as well as the Federal Trade Commission Act and the Guides for the Use of Environmental Marketing Claims.

6. Confidentiality -- The DTE regulations should add a blanket provision to protect confidential information.

We are unable to find any provision in the DTE draft regulations that reinforces the right of businesses to have confidential information protected. We recommend adopting a simple blanket provision to reassure market participants that information meeting the Massachusetts definition of protected information shall not be made public unless the original provider of said information consents to such disclosure or the information is aggregated or masked so as to avoid disclosure of trade secrets or competitively sensitive business and financial information. The California system has adopted such a blanket provision which might serve as a useful model for the DTE regulations.

7. Reasonable estimates of resource portfolio label information -- The DTE regulations could simplify the burdens of the initial phase of competitive markets by extending the period for which "reasonable estimates" can be used to calculate label information. The period should be extended to the first six months of operation.

We urge the DTE to consider amending Section 11.06(2)1(b)2 so that reasonable estimates may be used for the first six months of operation for the purpose of calculating the information that goes in the label. This slight modification recognizes that the new markets may open slowly and face a variety of unforeseen challenges. To ease the burden of dealing with this likely situation, an extension of the allowable time in which reasonable estimates may be used from three months, as currently drafted, to six months, might prove very

useful.